

Office of Historic Preservation:

**Did Not Always Comply With
Requirements for Sole-Source Contracts**

October 1996
95115

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October 2, 1996

95115

The Governor of California
President pro Tempore of the Senate
Speaker of the Assembly
State Capitol
Sacramento, California 95814

Dear Governor and Legislative Leaders:

Summary

The Bureau of State Audits reviewed the five sole-source contracts entered into by the Office of Historic Preservation (OHP) during fiscal years 1993-94 through 1995-96 and evaluated the OHP's compliance with relevant state contracting laws and regulations. Our review disclosed that the OHP sometimes failed to comply with the requirements for sole-source contracts. For example, the OHP did not always justify contract amounts or include market surveys in its requests for sole-source approval. In addition, we noted the OHP did not adhere to payment terms for two of the five contracts or comply with other legal requirements when planning and reviewing contracts. For instance, some of the contracts lacked essential elements, such as a progress schedule for contractor performance or a contractor's detailed budget. When the OHP does not adequately comply with sole-source contract requirements, it unnecessarily reduces the effectiveness of controls designed to protect the State's interests.

Background

The OHP, within the California Department of Parks and Recreation, assists the State in the preservation and stewardship of historical resources. The OHP is responsible for administering preservation programs set up by federal and state law. These programs, which are managed by a team of historians, archeologists, architects, and support staff, include the following:

- **Survey and Inventory:** The OHP provides guidance to communities conducting surveys of their historic resources and records the information in the statewide inventory of historic properties.
- **Information Centers:** The OHP administers the California Historical Resources Information System, which comprises 11 information centers throughout the State. The centers provide information on archeological and historical resources to local governments and individuals.
- **Registration:** In addition to reviewing nominations to the National Register of Historic Places, the OHP administers several state registration programs, including the California Register of Historical Resources, the State Registered Historical Landmarks, and the Points of Historical Interest.
- **Tax Credits:** For owners seeking tax credits for rehabilitating buildings listed on the National Register of Historic Places, the OHP certifies a building's significance and verifies that the work is being done in accordance with standards set by the Secretary of the Interior.
- **Grants:** The OHP distributes funds for historic preservation projects originating from the federal or state government or from voter-approved bond acts.
- **Certified Local Governments:** For local governments seeking to become certified local governments and thus become eligible for federal funds earmarked for them, the OHP assists with the application process and administers the grant funds.
- **Environmental Review:** The OHP reviews numerous federally assisted projects each year. In accordance with the National Historic Preservation Act of 1966, the OHP works with federal agencies to identify resources that may be eligible for listing on the National Register of Historic Places.

Scope and Methodology

The Joint Legislative Audit Committee requested that the Bureau of State Audits perform an audit of the sole-source contracts issued by the OHP during fiscal years 1993-94 through 1995-96. The purpose of our audit was to determine whether the OHP issued the contracts in compliance with

relevant state laws and regulations. We defined sole-source contracts as those contracts for which the OHP sought sole-source approval from the Department of General Services (DGS) or for which the OHP selected the contractor after evaluating fewer than three competitive bids.

To evaluate the OHP's compliance with the laws and regulations governing sole-source contracts, we reviewed the California Public Contract Code (PCC) and the State Administrative Manual (SAM) and identified the provisions and policies pertaining to this type of contract. We also obtained additional policies relating to sole-source contracts from OHP personnel.

To identify the sole-source contracts, we first reviewed all contracts awarded during fiscal years 1993-94 through 1995-96. The OHP entered into 22 contracts totaling approximately \$970,000 during this period. Of these, we identified five sole-source contracts, representing approximately \$622,000. We reviewed these five sole-source contracts for appropriate approval, cost justification, contract provisions, and supporting documentation.

***The Office of Historic Preservation
Sometimes Failed To Comply With
Requirements for Sole-Source Contracting***

During our review, we found that the OHP did not develop a justification of the contract amount for four of the five contracts. In addition, for one of the five contracts, the OHP did not include a market survey in its request for approval. The purpose of a market survey is to explain why similar services from other sources are unavailable or inappropriate to meet the OHP's needs.

Four of the contracts, for amounts ranging from approximately \$2,700 to \$20,000, did not require DGS approval because it had delegated the authority to approve certain contracts to the OHP; however, the OHP still needed to justify the reasonableness of the contract amounts and include those justifications in the contract files. Despite this requirement, we noted that for three of the four contracts, the OHP did not include such justification in the contract files. Upon our request, the OHP provided a justification for each of these contracts. Although the justifications appeared reasonable, we believe that developing and documenting justifications is an

important control within the contract planning process; therefore, the OHP should have prepared the justifications when it prepared the contracts.

The remaining contract exceeded the OHP's exemption amount and therefore was subject to DGS approval. This contract provided for emergency identification and evaluation of historic properties damaged by the 1994 Northridge earthquake. The OHP awarded the contract to a consulting firm that was knowledgeable in the professional standards applicable to identifying and evaluating historic properties and that was already located in the Northridge area. Although the initial contract was for only \$75,000, the OHP amended this contract three times, resulting in a total contract amount of \$580,000. The initial contract period was March 1994 through June 1994. The first amendment, prepared in March 1994, modified only the original scope of work; however, the second amendment, prepared in June 1994, extended the contract period through September 1994 and increased the contract amount by \$225,000. Finally, the third amendment, prepared in September 1994, extended the contract period until September 1995, modified the scope of work, and increased the contract amount by another \$280,000. Our review of this contract revealed that the OHP did not develop a justification of the contract amount or include a market survey in its request for sole-source approval from the DGS for either the initial contract or the second and third amendments.

Section 1236 of the SAM allows state agencies to award sole-source contracts if the DGS has agreed that only one source exists for the services and the Office of Procurement has approved the exempt request form, or if the director of the DGS determines that the State's interests are better served by using a sole-source contract. However, in these instances, the agencies must obtain appropriate management approval and provide a justification of the reasonableness of the contract amount whether or not the agency submits the contract to the DGS for approval. Furthermore, for sole-source contracts submitted to the DGS for approval, agencies must also include a market survey that explains why similar services from other sources are unavailable or inappropriate to meet the contract need or an explanation why a market survey would not be meaningful.

By not developing or including cost justifications or market surveys in its contract files and its requests for approval submitted to the DGS, the OHP cannot ensure that it does not curtail competition for the contract. Furthermore, through this curtailment, the OHP could pay more for services than necessary.

***The Office of Historic Preservation
Sometimes Did Not Adhere
to Contract Terms***

For three of the five sole-source contracts we reviewed, the OHP failed to adhere to various contract terms. For example, it did not always monitor contract payments to ensure compliance with contract terms. Specifically, for one contract totaling approximately \$20,000, the OHP did not withhold 10 percent of progress payments as required by the contract's terms. As a result, the OHP paid the contractor \$783 more for a progress payment than was allowable.

For another contract, totaling \$9,850, the OHP reimbursed the contractor for travel and per diem in excess of the amount allowable under the contract's terms. The contract provided for a travel and per diem rate of \$70 per trip; however, the contractor billed for expenses incurred that exceeded the per diem rate, and the OHP paid for them. As a result, the OHP overpaid the contractor by \$410. Finally, for a third contract, totaling \$580,000, we reviewed two invoices and found that the OHP did not require or retain adequate supporting documentation for \$675 of reimbursable expenses, such as photographs and duplication.

Section 1282 of the SAM requires departments to monitor compliance with contract terms to ensure that the State's interests are protected. Specifically, the contract manager responsible for approving invoices for payment should be familiar with the terms of the contract and the services to be provided. Without comparing the services received to the respective contract's requirements, the OHP may pay contractors for services that fail to meet the contract terms. When the OHP pays contractors without first obtaining adequate supporting documentation, it increases the risk that it will pay for unallowable costs or make duplicate payments.

***The Office of Historic Preservation
Did Not Always Comply With
Other Legal Requirements***

We found that the OHP did not always comply with legal requirements when planning and reviewing contracts. Specifically, we found that the OHP did not always include all the required elements in its contracts, review prior evaluations of contractors before awarding contracts, include resumes of

key contractors in the contract documents, or submit contractor evaluations to the DGS within 60 days after the contract was completed.

The OHP did not always adequately plan its contracting activities so that its contracts included all the elements necessary to effectively manage them. Specifically, we identified one sole-source contract for which the OHP failed to include both a progress schedule for contractor performance and the contractor's detailed budget. Section 10371 of the PCC and Section 1283 of the SAM require that contracts totaling more than \$1,000 contain certain fundamental elements. Two of these elements are a progress schedule for contractor performance and the contractor's detailed budget. These two elements enable the OHP to ensure that the contractor provides services within an acceptable time frame and that the contractor's billings are consistent with the services contracted for. Because the OHP did not include these elements in the contract terms, it cannot ensure that the contractor is providing the services within an acceptable time frame or whether the amounts the contractor is charging are reasonable.

For two contracts we reviewed, the OHP did not review contractor evaluations on file with the DGS before awarding the contracts. Section 10371 of the PCC and Section 1281 of the SAM require agencies to review any contractor evaluations on file with the DGS before awarding contracts totaling \$5,000 or more. By not reviewing prior contractor evaluations, the OHP may award a contract to a contractor that provided substandard services in the past.

In addition, for three of the contracts we reviewed, the OHP did not include in the contract documents the resumes of the key contractors performing the services. Section 10371 of the PCC and Section 1281 of the SAM require that the OHP include resumes of the key contractors as part of the contract before awarding the contract. By not reviewing resumes of potential contractors, the OHP cannot ensure that it selected the key contractor with the best qualifications to satisfactorily complete the contract.

Finally, we found that the OHP did not complete post evaluations within 60 days after the contract was completed for two contracts although these evaluations are required by Section 10369 of the PCC and Section 1283 of the SAM. Specifically, the PCC and the SAM require that the OHP complete a post evaluation of the contractor within 60 days after the contract is completed for each consulting contract totaling \$5,000 or more. By not completing the contractor

evaluations within the allotted time, the OHP unnecessarily diminishes the effectiveness of controls designed to protect the State's interests in awarding future contracts.

Conclusion

The OHP sometimes failed to comply with state laws and regulations pertaining to sole-source contracts. Specifically, it did not develop cost justifications for contract amounts as part of the contract planning process or include market surveys in its requests for sole-source approval from the DGS. In addition, the OHP did not always adhere to contract payment terms or require contractors to provide adequate documentation to support invoiced amounts. Sometimes the OHP also failed to adequately plan contracts to include the essential elements of a contract, such as progress schedules and contractors' detailed budgets, or include key contractor resumes in the contract files. Furthermore, the OHP did not always review contractor evaluations before awarding contracts, nor did it promptly prepare post evaluations after the contracts were completed. When the OHP does not adequately comply with sole-source contract requirements, it unnecessarily reduces the effectiveness of controls designed to protect the State's interests. By not adequately planning, monitoring, and evaluating contracts, the OHP cannot ensure that state resources are used efficiently and effectively.

Recommendations

The OHP should comply with all state laws and regulations pertaining to sole-source contracts.

For contracts exempt from DGS review and approval, the OHP should develop cost justifications and include them in the contract files.

For contracts that require DGS approval, the OHP should include in the request for approval a cost justification and a market survey.

Finally, to ensure that payments are made in accordance with contract terms, the OHP should request detailed support for invoices from contractors and compare invoices to specific contract terms.

We conducted this review under the authority vested in the state auditor by Section 8543 et seq. of the California Government Code and according to generally accepted governmental auditing standards. We limited our review to those areas specified in the audit scope of this report.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Kurt Sjoberg", written in a cursive style.

KURT R. SJOBERG
State Auditor

Staff: Elaine M. Howle, CPA, Audit Principal
Doug Cordiner
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DEPARTMENT OF PARKS AND RECREATION

P. O. BOX 942896

SACRAMENTO, CA 94296-0001



September 25, 1996

Kurt R. Sjoberg
State Auditor
Bureau of State Audits
660 J Street, Suite 300
Sacramento, CA 95814

Dear Mr. Sjoberg:

Thank you for the opportunity to respond to your September 19, 1996, memorandum to Secretary Wheeler, conveying the draft audit report on sole-source contracts awarded by our Office of Historic Preservation (OHP). Secretary Wheeler has asked that I relay our comments to the draft audit report.

It has always been and will continue to be the intent of the OHP to comply with laws and regulations associated with the initiation and implementation of all contracts. The OHP staff involved on contracts acted in all cases to the best of their ability and knowledge of the State contract process. Based on your report, the OHP will pursue further training for staff and develop safeguards to implement your recommendations.

Of the five sole-source contracts reviewed, two contracts, including the first and largest, were made in response to the Northridge Earthquake. For these contracts sole-source approvals were sought and received from the Department of General Services (DGS). Another contract was awarded pursuant to a formal advertising and receipt of bids. A single bid was received and the contract was issued in accordance with Section 10340 (b) (2) of Public Contract Code. This code section states, *"Three competitive bids or proposals are not required in any of the following cases: When the agency awarding the contract has advertised the contract in the California State Contracts Register and has solicited all potential contractors known to the agency but has received less three bids or proposals."* Another contract was awarded to a consultant to continue a conflict resolution process begun by a previous consultant that had resigned. The final contract involved an Agreement for Services which staff understood to be the correct method for acquiring the services of the consultant since no other known consultants with the required expertise were available.

The following includes the recommendations made in the audit report (**in bold type**) followed by our response in regular type.

Recommendations

"The OHP should comply with all state laws and regulations pertaining to sole-source contracts." The OHP acknowledges this requirement and has always sought to comply with all state laws and regulations pertaining to sole-source contracts. We believe that the instances where OHP failed to comply are isolated cases and do not represent the norm. Nevertheless we will review our process and make the necessary changes to achieve consistent compliance with all contract requirements in the future.

"For contracts exempt from DGS review and approval, the OHP should develop cost justifications and include them in the contract files" As noted in your report, *"Upon our request, the OHP provided a justification for each of these contracts."* Cost justifications are developed as part of our contract process and existed for the contracts in question. However they were not adequately documented and included in the contract files. The OHP will ensure that cost justifications are clearly documented and included in all future contracts files.

"For contracts that require (DGS) approval, the OHP should include in the request for approval a cost justification and market survey." Only one of the five sole-source contracts required DGS approval. OHP obtained DGS approval for this contract based on the urgent need to identify, evaluate, and provide appropriate consideration to historic properties damaged by the Northridge Earthquake. For cost justification the OHP relied on the Federal Emergency Management Agency's (FEMA) cost estimates for this earthquake and on consultants they had retained in similar situations. This is the first time OHP had initiated a contract related to a natural disaster and relied on DGS to inform us of contract requirements. When the contract was approved by DGS, OHP assumed that all requirements were met. In the future the OHP will ensure that a market survey is completed for all appropriate contracts. In instances where a market survey would not be meaningful, the OHP will ensure that an explanation is properly documented.

"Finally, to ensure that payments are made in accordance with contract terms, the OHP should request detailed support for invoices from contractors and compare invoices to specific contract terms." It is our normal process to require detailed support for invoices. The one invoice identified in the report dealt with copying records and photographs taken to document the historic properties affected by the Northridge Earthquake. The costs appeared reasonable given the type of work being conducted. Nevertheless, in the future OHP will ensure that all invoices contain detailed support.

We agree that in two instances the OHP did not adhere to contract terms in authorizing payments on invoices. In one contract the OHP did not withhold 10 percent of progress payments as required by the contract terms. This is an isolated instance where the individual who reviewed the invoice was not aware that the 10% withholding applied to each invoice. While this resulted in the contractor receiving full payment for a progress billing, ultimately the contractor did not receive more than the approved contract amount and the services contracted for were received.

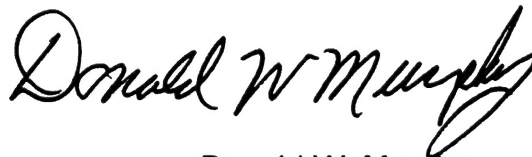
Since that time we have conducted training for staff members in the proper processing of invoices. In the second contract the terms of the contract were misunderstood. This resulted in an overpayment. The contract in question was executed by the Department's Administration Division on the behalf of the OHP, which resulted in our misinterpretation of the payment terms leading to an overpayment. Furthermore, when the contract was drafted, it was not anticipated that it would be necessary for the consultant to spend more than one day at a time. In retrospect, when this became evident, an amendment should have been initiated to allow for lodging. This is specially true since, from a cost basis, it was in the best interest of the State to allow for lodging. In the future, all authorized contract payments by the OHP will be verified by a manager/supervisor prior to release to ensure accuracy.

Finally, OHP will improve its procedures for the issuing and monitoring of all its contracts. To that end we propose to provide staff with training on State contract laws, policies and procedures, and to develop a checklist of contract terms for all OHP contracts. This checklist will require the signatures of program staff, and the fiscal manager. A similar checklist is currently used for all OHP Federal grants.

In closing we appreciate the opportunity to respond to the draft report. We also appreciate the helpfulness and professionalism demonstrated by Marianne Marler and Elaine Howle of your staff. This audit came at a time when OHP was processing two sets of grants applications involving more than 150 applicants. Despite the heavy workload, the OHP attempted to fully comply with requests made by your staff. We look forward to reading the final report, but will not wait to take corrective measures identified in the report.

As requested this response is also copied on the enclosed diskette using a PC compatible file in the text ".txt" format.

Sincerely,

A handwritten signature in black ink, reading "Donald W. Murphy". The signature is fluid and cursive, with the first letters of each word being capitalized and prominent.

Donald W. Murphy
Director

Enclosure

cc: Douglas P. Wheeler
Secretary for Resources

cc: Members of the Legislature
 Office of the Lieutenant Governor
 Attorney General
 State Controller
 Legislative Analyst
 Assembly Office of Research
 Senate Office of Research
 Assembly Majority/Minority Consultants
 Senate Majority/Minority Consultants
 Capitol Press Corps